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Article (Published Version)

Szyszczak, Erika (2016) Article 263(4) TFEU and the impossibility of challenging recovery decisions in state aid: annotation on the judgments of the general court of 15 September 2016 in T-219/13 Pietro Ferracci v European Commission and T-220/13 Scuola Elementare Maria Montessori v European Commission. *European State Aid Law Quarterly*, 15 (4). pp. 637-641. ISSN 1619-5272

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Article 263(4) TFEU and the Impossibility of Challenging Recovery Decisions in State Aid

Annotation on the Judgments of the General Court of 15 September 2016 in T-219/13 *Pietro Ferracci v European Commission* and T-220/13 *Scuola Elementare Maria Montessori v European Commission*

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The Ferracci and Montessori judgments of the General Court of 15 September 2016 were challenges brought against a Commission Decision scrutinising Italian municipal tax rules allowing tax exemptions for non-commercial bodies. The cases raise issues of when third party standing is allowed under Article 264(4) TFEU, the standard of review of European Commission Decisions, the concept of economic and non-economic activity and when the European Commission may decide that it is impossible for a Member State to recover illegal State aid.

Key Words: Economic and Non-Economic Activity; Access to Justice; Standing before the General Court; Impossibility of Recovery of State Aid.

I. Introduction

The *Ferracci* and *Montessori*¹ judgments of the General Court of 15 September 2016 were challenges brought against a Commission Decision² scrutinising Italian municipal tax rules allowing tax exemptions for non-commercial bodies. The applicants had made earlier complaints in 2006 arguing that illegal State aid was present in the Italian provisions which granted an exemption from the municipal tax on real estate and a corporate tax reduction

to entities that were seen as non-commercial entities (including ecclesiastical bodies) and as such were deemed not to be carrying out economic activities.

The European Commission found that certain tax exemptions did not constitute State aid, but in one instance an exemption was found to constitute unlawful State aid where it related to activities involving real estate and the entities were engaged, in part, in economic activities. But, for technical reasons the European Commission found that this was an exceptional case and that it was impossible for Italy to recover the illegal State aid.

The judgments cover a wide range of State aid issues, making them noteworthy. The most important aspect is the outcome: that even when aggrieved third parties are able to satisfy the strict standing provisions of Article 263(4) TFEU, the European Courts are still very reluctant to interfere with the European Commission's powers to interpret and implement the State aid provisions. The rulings also raise issues of how the European Commission and the General Court address the economic/non-economic activity bright line which determines when the economic rules of the TFEU apply, espe-

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DOI: 10.21552/estal/2016/4/11

1 Case T-219/13 *Pietro Ferracci v European Commission* [2016] ECLI-485. On appeal: Case C-624/16 P. See also T-220/13 *Scuola Elementare Maria Montessori v Commission* [2016] ECLI-484. On appeal: Case C-622/16 P and Case C-263/16 P.

2 European Commission, Decision of 19 December 2012 on State aid SA.20829 (C 26/2010, ex NN 43/2010 (ex CP 71/2006)), Scheme concerning the municipal real estate tax exemption granted to real estate used by non-commercial entities for specific purposes implemented by Italy, available at: <<http://curia.europa.eu/juris/document/document.jsf?text=&docid=183333&pageIndex=0&doclang=FR&mode=lst&dir=&occ=first&part=1&cid=155618>> Last accessed on 6 December 2016.

cially where State aid may be present, and, finally, the question of when illegal State aid is not capable of recovery. These aspects of the judgments are remarkable since they appear to go against the grain of current European Commission decision-making and European Court jurisprudence. This annotation addresses the three main issues of: first, *locus standi* of third parties before the European Courts; second, the line between economic and non-economic activity in determining when the State aid rules apply; third, the rules on when it is impossible for a Member State to recover illegal State aid.

II. Access to Justice: Article 263(4) TFEU

Access to justice is viewed as a fundamental right in EU law. Recent years have seen a growth in challenges to the behaviour and exercise of powers of the European Commission in competition law cases using fundamental rights concepts.³ This reliance on fundamental rights concepts is facilitated by specific procedural rules and guarantees in Regulation 1/2003⁴ and, it is arguable, that the recent resort to fundamental rights concepts is making some inroads into the wide discretion normally attributed to the European Commission to investigate breaches of competition law in the EU.⁵ In State aid litigation the focus of access to justice litigation is slightly different in that the legal issues usually concern third party (usually competitors) rights to challenge European Commission State aid Decisions, and their task is often made easier when they have initiated complaints and participated into the formal procedures and investigative process. In cases where such participation in the stages of the formal procedures is not prominent, it is difficult for third parties to challenge European Commission Decisions.

III. The Standing of Third Parties to Challenge European Commission Decisions

The Treaty of Lisbon 2007 attempted to liberalise the narrow rules of standing found in the original EEC Treaty which applied to natural and legal persons to challenge acts of the EU Institutions. This aim was

implemented by amending Article 263(4) TFEU to allow any natural or legal person to institute proceedings against a regulatory act which is of *direct* concern to them and does not entail implementing measures:

"Any natural or legal person may, under the conditions laid down in the first and second paragraphs, institute proceedings against an act addressed to that person or which is of direct and individual concern to them, and against a regulatory act which is of direct concern to them and does not entail implementing measures."

At face value this new wording eases up on the earlier requirement for an applicant to show, the almost impossible, requirement that a regulatory act is of individual concern according to the *Plaumann* formula.⁶ But there is still the requirement to show the applicant is *directly* concerned by a measure.

Post-Lisbon applicants have not had much success in satisfying this new element of the standing test. In relation to State aid acts the CJEU has dismissed the application on various grounds. For example, in *Mory*⁷ the Court found that the decision was not an act of general application. In other cases such as *Telefonica*⁸ the Court found that implementing measures

3 Greater reliance of fundamental rights concepts in legal proceedings is also triggered by the criminalisation of anti-competitive behaviour at the national level.

4 The most prominent fundamental rights provisions in EU law are found in the Charter of Fundamental Rights of the European Union, OJ C 326/ 02. The provisions which are relevant for challenging European Commission Decisions in competition law are the following: Article 7 (respect for private and family life, equivalent to Article 8 ECHR); Article 16 (freedom to conduct a business); Article 17 (equivalent to A1P1 ECHR); Article 41 (right to good administration); Article 47 (right to effective remedy and to fair trial); Article 48 (presumption of innocence; respect for rights of defence); Article 49(3) (proportionality of criminal penalties).

5 See, for e.g. the judgment of the ECtHR of September 2011 *Menarini Diagnostics v Italy*, No 43509/08; Case C-272/09 P *KME Germany AG v Commission* [2011] ECLI-810; Case C-386/10P *Chalkor v Commission* [2011] ECLI-815; Case C-199/11 *Europese Gemeenschap v Otis NV and Others* [2012] ECLI-684.

6 Case C-25/62 *Plaumann & Co. v Commission of the European Economic Community* [1963] ECLI-17. In State aid cases it makes a huge difference whether the third party applicant is challenging a European Commission Decision at the phase 1 Decision, or as is the case of *Ferracci and Montessori*, at the phase 2 stage of challenge after the formal Decision has been taken. At this stage the applicant becomes an interested third party where the restrictive *Plaumann* formula applies.

7 Case C-33/14 P *Mory v Commission* [2015] ECLI-609.

8 Case C-274/12 *Telefonica v Commission* [2013] ECLI-852.

were required.⁹ Thus, *Ferracci* and *Montessori* are rare cases where the new admissibility criteria of Article 263(4) TFEU were satisfied.

Article 263(4) TFEU was satisfied because there was a regulatory act to challenge that was legally complete. The General Court held that the Italian measures were applicable to situations determined objectively with legal effects for general categories of undertakings; the Commission Decision was of general application and could be classified as a regulatory act. The General Court also took into account the fact that the European Commission's Decision was final and binding upon Italy, and did not entail any implementing measures.

On the direct concern point the General Court found that the applicants could show that they were *directly* concerned by the contested Decision because of their competitive relationships with the undertakings which were the beneficiaries of the contested tax exemptions.

IV. Economic and Non-Economic Activity

The legal issue of determining the bright line between economic and non-economic activity arose in the context of the extent of the recovery of illegal State aid. In order to obtain tax exemptions, a non-commercial entity had to show that it was engaged in non-economic activities. However, the Italian system did not create a structure where a beneficiary of the tax concession was able to show the mix of eco-

nomic and non-economic activities. Overall, the Italian authorities argued that the entities in question were not undertakings because their activities mainly targeted very specific categories of recipients. The activities did not constitute an offer of goods or services on the market and thus were not in competition with the activities carried out by commercial undertakings. In most cases the activities had specific social characteristics, for example, they were performed in the public interest or for solidarity purposes, were either free of charge or services were provided for reduced fees. The European Commission was not able to discern if, or what proportion of, the previous activity was economic or non-economic. In this situation it was not possible for the European Commission to find positive evidence that there was economic activity taking place in the past and that the tax concessions gave an undertaking a selective advantage for the purposes of satisfying the State aid rules.¹⁰

The General Court examined the reform of the exemption in Italian law which tightened up the tax exemptions by applying them to only non-economic activities. As recent case law and Decisions of the European Commission reveal, it is not easy to apply a clear bright line to non-economic activities, especially where there are mixed economic and non-economic activities and where an entity is able to ask for payment for any ancillary services provided.¹¹ In the *Montessori* case the entities were allowed to charge small, or nominal, amounts for their services, and economic activities were not prohibited.

9 In other cases the CJEU has applied this wording strictly. See Case C-456/13 *P T and L* where Regulations setting out exceptional import tariffs on sugar left no implementing discretion to the national authorities but the CJEU held that the Regulations produced legal effects only through the intermediary of the acts of the national authorities. See also: Case C-132/12P *Stichting Woonpunt*, [2014] ECLI-100; Case T-276/13 *Growth Energy* [2016] ECLI-340; Case T-57/11 *Castelnuovo*, [2014] ECLI-1021; Case T-614/13 *Romonta* [2014] ECLI-835; Case T-287/11 *Heitkamp* [2016] ECLI-60. See also Case C-541/14 P *Royal Scandinavian Casino v Commission* [2016] ECLI-302 and Case T-238/14 *EGBA and RGA v Commission* [2016] ECLI-259. This line of case law suggests that the Treaty of Lisbon 2007 amendment has not increased access to the Court of Justice of the European Union, and indeed may be even more difficult to satisfy than the pre-Lisbon test.

10 *Montessori* (n 1), [106].

11 See, for example EC Decision SA 27301. Here the European Commission accepted that Dutch Nature Management Organisations (NMO) were not involved in economic activities when they were carrying out their nature conservation tasks, but that rev-

enue generating activities of the NMO were economic activities and this made the NMO undertakings carrying out an economic activity. See E Szyszczak, 'Survey Services of General Economic Interest and State Measures Affecting Competition' (2016) 7 (7) *Journal of European Competition Law & Practice*, 501. Some guidance on what proportion of ancillary economic activity of a non-commercial entity is acceptable is now found in the procurement rules, for e.g. Article 12 of Directive 2014/24, OJ 2014 L 94/65 allows in-house entities to develop 20% of their services or goods in the market and still be considered under the control of the contracting authority for the purposes of the direct award of contracts. Whether this excludes the existence of State aid or not is unclear: for a critical discussion, see G Skovgaard Ølykke and C Fanø Andersen, 'A State Aid Perspective on Certain Elements of Article 12 of the New Public Sector Directive on In-house Provision' (2015) 1 *Public Procurement Law Review*, 1; G Skovgaard Ølykke, 'Commission Notice on the Notion of State Aid as Referred to in Art. 107(1) TFEU: Is the Conduct of a Public Procurement Procedure Sufficient to Eliminate the Risk of Granting State Aid?' (2016) 5 *Public Procurement Law Review*, 5197. [My thanks to Albert Sanchez-Graells for discussing this point with me].

The Court reiterates its position that the fact that the supply of goods and services is made on a non-profit basis does not prevent the supplier from being considered as an undertaking where it competes with other operators who pursue profit.¹² The Court also noted that new tax rules were introduced to ensure that if the property was for mixed use, the tax exemption applied only to the part of it which was used for non-economic activities.¹³

The Court took a formal approach to identifying a set of indicators which were evidence that the tax exemption could apply to non-economic activities. These indicators included the not-for-profit nature of the activities,¹⁴ the fact that the entities were not inherently in competition with undertakings operating on a for-profit basis. Other indicators were drawn from an examination of the statutes of the entities. For example, the statutes prohibited the distribution of some profits (or operating surpluses); any profits had to be reinvested in activities that contributed to social solidarity. Where a non-commercial entity was dissolved its assets had to be transferred to another non-commercial entity.

In the *Montessori* case, where entities operated in the education sector, specific conditions were imposed: the activities had to be of a quality comparable to that of public education and the school had to operate a non-discriminatory entry policy for students; a school had to accommodate students with disabilities; the school had to provide for the publication of its accounts; education had to be provided free of charge or for a nominal amount covering only a proportion of the actual cost of the service.¹⁵

The General Court emphasises the commercial negotiation side of remuneration when it constitutes consideration for a service. This aspect of negotiation is missing in the provision of a national system of universal education. Thus, in the situation in *Montessori*, the ecclesiastical bodies were not acting in a commercial sense but merely fulfilling public duties towards the population. The nature of the activity was not affected by the fact that pupils *occasionally* were asked to pay certain fees in order to contribute to some extent to the system's operating costs.¹⁶ This aspect of the ruling shows the tension between the EU level approach of defining an undertaking and economic activity according to a functional set of criteria and what appears to operate in practice; deciding cases in the national context in determining whether there is a market and that economic activity takes place.

V. Impossibility of Recovery of Illegal State Aid

As is often the case, having opened the door to access the Court the door was quickly slammed shut in dismissing the substantive grounds of appeal. The General Court confirmed that the European Commission could make a finding of impossibility of recovery in the final Decision where a Member State had explained the reasons for such a conclusion during the formal investigation.

In finding that the European Commission had not erred in deciding that Italy could not, and therefore should not, recover the illegal State aid at the formal investigation stage of the procedure the General Court upholds the European Commission Decision not to order the Member State to attempt recovery of the State aid. In previous case law a Member State that pleads 'absolute impossibility' normally has to show that it has tried to recover the aid.¹⁷ The reasons adduced as to why impossibility arises have varied from constitutional to political reasons. What is unusual in the *Ferracci* and *Montessori* cases is that the impossibility of recovery arises because it was a fault of the Italian administrative system that did not foresee the need to separate out economic and non-economic activities for tax purposes in the creation and administration of the public registers and data bases. The Italian system did not impose any obligations upon the non-commercial entities to separate out their activities, or even to show that they satisfied the basic rule that their operations were primarily non-economic in order to qualify for the tax exemptions.¹⁸ The Italian tax register and data base were structured in such a way that it would be im-

¹² *Montessori* (n 1), [133].

¹³ *Montessori* (n 1), [135].

¹⁴ But see also Case AT.39759 – ARA Foreclosure, published 11 October 2016 where an Austrian waste management company operating on a non-for-profit basis was held to be an undertaking for the purposes of Article 102 TFEU. Here a competitive market was likely to materialise if the dominant entity had not prevented access to the infrastructure.

¹⁵ *Montessori* (n 1), [136-141].

¹⁶ *Montessori* (n 1), [141].

¹⁷ See H Hofmann and C Micheau, *State Aid Law of the European Union* (OUP 2016), Part IV (3) and page 395: "There is a well-entrenched praetorian *obiter dictum* in this respect, according to which a Member State may not plead provisions, practices or circumstances existing in its internal legal system in order to justify a failure to comply with its obligations under EU law."

¹⁸ *Montessori* (n 1), [95-100].

possible to identify retroactively the nature of the activities that were being carried on at the specific location in order to determine whether the tax exemption should have applied. In paragraph 106 (*Montessori*), the General Court makes a potentially far-reaching point in cases where it is difficult to separate out economic and non-economic activities, the European Commission cannot assume a presumption of State aid. Yet, this seems to be what the European Commission did in this case.

The General Court agreed with the European Commission that the latter could not impose obligations on a Member State to recover illegal State aid where objectively, and absolutely, it was impossible to implement the obligation.¹⁹ In so doing, the General Court appears to see this as a difficult case, where the ruling is based upon the specific factual situation, since the Court confirmed the existing case law that it does not amount to absolute impossibility to argue that recovery may be difficult due to political, legal or practical reasons,²⁰ or due to the high number of aid recipients.²¹ The deference shown to the European Commission by the General Court is quite remarkable. In deciding upon the impossibility to recover point, the European Commission does not have a margin of discretion to work with, which is protected by a limited judicial review (as is the situation when assessing the compatibility of State aid with EU law). Rather the impossibility issue is an objective notion that should be subject to full judicial control by the General Court. Thus the question arises as to whether this situation in Italy is an example of an objective justification to satisfy the impossibility standard, setting a precedent, or whether the General Court is applying a different standard of review of the European Commission powers as regards the determinants of the impossibility to recover State aid.

The General Court reached this position because neither the public register of land ownership, nor the tax databases allowed the tax authorities to identify whether the activity was economic or non-economic,

even where the entities were themselves not classified as commercial entities. The tax exemption provisions applied to *all* of the activities of non-commercial entities, when they were carrying out primarily non-economic activities.

This formal approach to categorising non-economic activity appears to go against the grain of the established case law which looks to function over form. These cases are unusual, but are part of increased instances of examples where hybridisation and commercialisation of public and non-economic entities may in fact involve an element of mixed activities, or where the State starts to charge for services previously offered as free, public goods, which may change the nature of the activity for the purposes of EU economic law. Each case appears to turn on its own facts, with an inquiry as to the nature of the activity of the entity primarily fulfilling public and/or social functions.

The Court also dismissed the challenges to the findings that there was no State aid. Particular attention is paid to the legal situation of the ecclesiastic exemptions. The GC placed emphasis upon the formal requirement that under Italian law, ecclesiastical institutions could only retain their status if they did *not* carry out commercial activities.

VI. Conclusions

The rulings in *Ferracci* and *Montessori* are instructive of how the door to the European Courts can be edged open for third parties to register complaints on how the European Commission has conducted a State aid investigation. But, unsurprisingly, they do not offer up any hope that the European Courts will interfere with the role of the European Commission, especially its discretion to determine what is legally possible and practicable when it comes to recovery of State aid. It is also interesting that the Court was not willing to pursue a broad effects-based approach to the impact of the tax exemptions in what was a competitive market, but was willing to go along with upholding a form-based national approach where historical attachments to principles of solidarity play a significant role in determining the line between economic and non-economic activities.

¹⁹ *Montessori* (n 1), [83].

²⁰ *Montessori* (n 1), [91].

²¹ *Montessori* (n 1), [92]. See Case C-441/06 *Commission v France* [2007] ECLI-616; Case C-214 *Commission v Italy* [2005] ECLI-440.